TEACHER PENSION TENSION

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K-12 public school teachers in Missouri have likely noticed that their pensions have become a source of tension. The Missouri Public School Retirement System (MPSRS) faces financial problems that require fundamental change. This is an opportunity to explore alternative teacher compensation packages that would give Missouri a strategic advantage in new teacher recruitment.

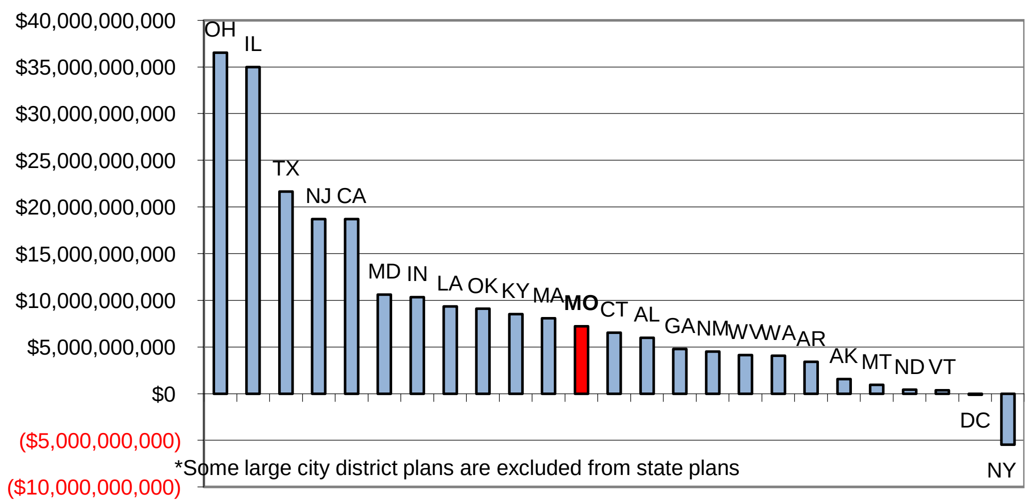
Defined Benefit Retirement Plans
MPSRS is a defined benefit pension plan, which means that it promises a specified monthly benefit upon retirement that is predetermined by a formula based on earnings history, tenure of service and age. Most private sector employees now have defined contribution plans (if they have any retirement plan at all). Defined contribution plans provide the individual an account for benefits based solely on the amount contributed to the participant's account, which can then earn interest sheltered from income taxes until the individual retires.

What is the Problem?

If you a current teacher, you are likely counting on pension income upon retirement. Perhaps you have even calculated your expected pension income based on your years of service and current/future salary. So what is the tension? The tension is over the current unfunded liability of MPSRS. Although the market value of the MPSRS assets was over $28 Billion on June 30, 2009, this value is not nearly enough to cover promises made to current and future retirees.[1] As of June 30, 2009, the MPSRS unfunded liability was $7.2 Billion.

The MPSRS large unfunded liability is not unusual. As Chart 1 demonstrates, most state teacher retirement plans face staggering shortages.

Chart 1: Unfunded Liabilities for State Teacher Pension Plans



Source: NASRA Pension Survey, 2009

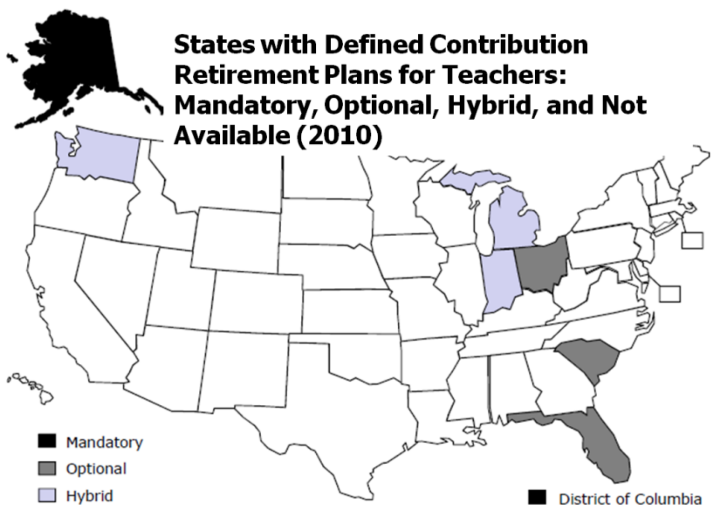
[1] Source: *2009 Public Fund Survey.* The survey is sponsored by the National Association of State Retirement Administrators and the National Council on Teacher Retirement (http://www.publicfundsurvey.org).

Missouri is in the same boat as many states. Unfortunately, this boat is sinking. A $7.2 Billion unfunded liability is not solely a matter of a few unfortunate years in the stock market or baby boomer age demographics (although these factors do not help). Rather, MPSRS must be restructured to meet its promises to teachers.

How Did it Get Like This?

Promising generous pensions to teachers is a method of improving teacher compensation. The perception has long been that teachers are underpaid. By providing strong pensions, the state can combat teacher shortages and improve teacher retention. It is interesting to consider the retirement programs for teachers across the country. The research is sparse on the effectiveness of retirement programs on teacher attraction and retention. As Chart 2 shows, most states have similar Defined Benefit plans, and therefore it is difficult to determine if these plans provide a workforce attraction and retention advantage.

Chart 2: Structures of Teacher Retirement Plans[2]



The states in white all offer defined benefit retirement plans. The characteristics of these plans differ in the following ways:

- Benefit Multiplier (multiplied by number of years of service to generate percentage of salary provided as retirement benefit);
- Teacher Contribution to Retirement Plan (as a percentage of teacher's total compensation);
- Employer (School District) Contribution to Retirement Plan (as a percentage of each teacher's total compensation).

The following charts compare MPSRS to other state teacher pension systems according to these variables.

[2] Snell, Robert. *State Defined Contribution and Hybrid Pension Plans.* National Conference of State Legislators, June 2010.

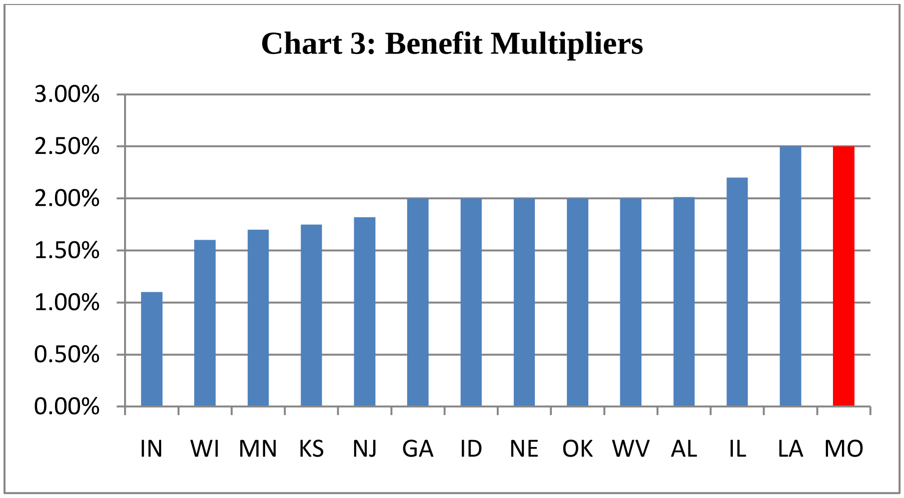


Chart 3: Benefit Multipliers
3.00%
2.50%
2.00%
1.50%
1.00%
0.50%
0.00%
IN WI MN KS NJ GA ID NE OK WV AL IL LA MO

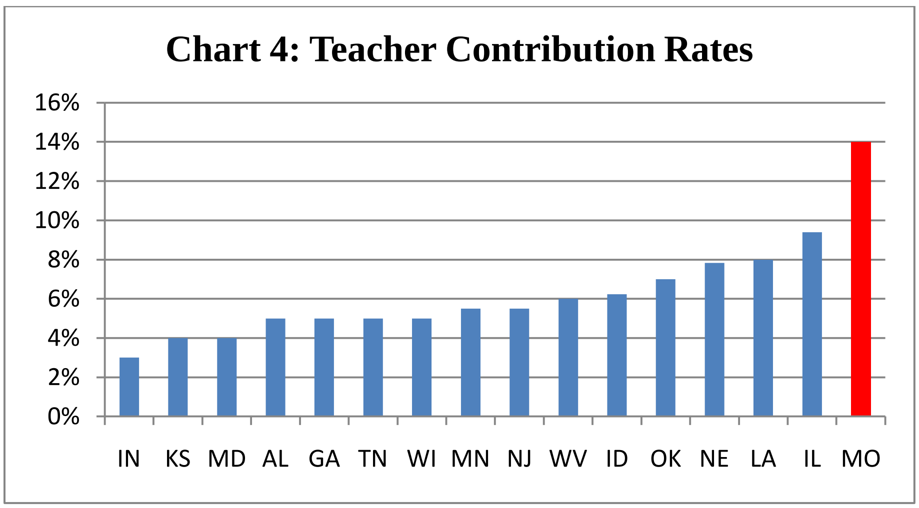


Chart 4: Teacher Contribution Rates
16%
14%
12%
10%
8%
6%
4%
2%
0%
IN KS MD AL GA TN WI MN NJ WV ID OK NE LA IL MO

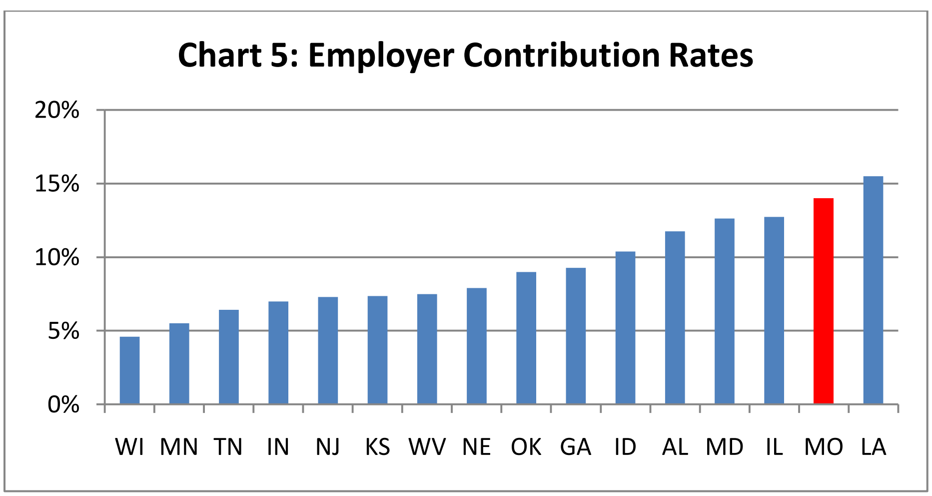


Chart 5: Employer Contribution Rates
20%
15%
10%
5%
0%
WI MN TN IN NJ KS WV NE OK GA ID AL MD IL MO LA

When compared to other state teacher retirement plans, MPSRS has:

- A high benefit multiplier (2.5);
- A high teacher contribution rate (14%); and
- A high employer contribution rate (14%).

Social Security
Teachers that are in MPSRS are not eligible for Social Security. They do not pay Social Security payroll taxes and cannot collect Social Security benefits.

Missouri teachers contribute a high percentage of their salary into the pension system. Fourteen percent of teacher salaries go into MPSRS, which is then matched by the school district. This amount is set to rise to 14.5 percent in 2011.

Legal Issues

Current teachers and retirees likely will not see their pensions reduced. Since pensions are essentially guaranteed by teacher contracts, cutting benefits for those already in the system would pose some legal obstacles. Therefore, any changes that are made will have to be made for future teachers.

Current Plan

A proposal from MPSRS would cap teacher contribution rates at 15 percent for teachers already in the system and 12 percent for new teachers. These new teachers would receive reduced pensions upon retirement:

- The benefit multiplier would be reduced from 2.5% to 2%;
- The Retirement age would be raised from 60 to 62.

MPSRS administrators intend to develop consensus from teachers and then take their draft to legislators in 2012[3].

Proposed Action: Find out what Missouri's Future Teachers Want

Since changes to the pension system would primarily affect future teachers, it would make sense to ask them what they want. In other words, what forms of compensation would be most attractive? By restructuring retirement plans for future teachers in a way that is more fiscally sound, it is possible that Missouri could make the teaching profession more attractive.

For example, suppose that teacher contribution rates to MPSRS were gradually reduced over several years while employer contribution rates were also reduced. Teacher take home pay would then rise and district contributions could be gradually converted into higher salaries. Immediate teacher compensation would increase sharply, potentially making the teaching profession more attractive in Missouri. This is not a formal proposal, and merely suggests a possible alternative. It is noteworthy that nobody has asked future teachers what they would like in terms of a total package of compensation.

I propose that the Missouri Department of Economic Development commission a study researching the structure of compensation packages that future teachers would prefer.

[3] Young, Virginia. *Future Missouri Teachers' Pensions Likely to be Smaller*. St. Louis Post-Dispatch, September 8, 2010.